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SUBJECT: EXPERTS DISCUSS AUSTRALIA-CHINA ECONOMIC
RELATIONSHIP

¶1. (SBU) Summary: The consensus among several of the leading Australian economic thinkers in Canberra is that the commodities boom will begin to cool off, but that Chinese and other developing market economic growth will continue to prop up Australian export strength over the long run. Australians are concerned about the motives behind Chinese investment in the resources sector, but China is only the latest outsider to want to control a piece of the pie. End Summary.

¶2. (SBU) At a lunch hosted by the Charge d'Affaires on July 30, Dr. Steven Kennedy, Chief Macroeconomist Advisor from the Prime Minister's Office; Rio Tinto's Lyall Howard (nephew of former PM John Howard); Peter Downes, Principal Macroeconomist at the Center for International Economics; and John Hogan, the head of the Australian Bureau of Agriculture and Resource Economics (ABARE) Agriculture & Trade Branch discussed Australia's economic relationship with China, the PRC's dependency on Australian commodities and Australians' views on foreign direct investment in Australia.

FTA: Services are Crucial

¶3. (SBU) Kennedy mentioned that Australian financial services firms remain very interested in expanding in China, and an Australia-China FTA should present itself as an opportunity to access the Chinese market. However, all at the table agreed that China had fallen short so far on the level of reciprocity it was prepared to accept. No one at the table saw any possibility of a quick breakthrough on services or other issues in the next round of negotiations.

Commodity Prices To Cool Off, But Trend Up

¶4. (SBU) Downes said his Centre's prediction was that Australian commodity prices in the short term would come back from record-breaking prices to a more modest level, probably around \$40 per ton for iron ore, for example, by about 2013, compared with spot prices in China that have gone as high as \$200 per ton this year. However, given the inability of the government in China to restrain infrastructure investment, long-term demand would remain strong and push prices up. Both Kennedy and Howard agreed with Downes that commodity prices would contract soon, but trend higher over the long term. Kennedy felt that the recent failure to reach an agreement in the Doha round would shake somewhat global business confidence and could further influence a downward commodity price shift. Howard said that Rio would welcome the price fall as the drop in prices will sift out the "predatory" newcomers that have popped up in the sector and

allow Rio to regain a larger share of the market. Hogan stated that ABARE also forecasts a drop in prices but sees the long term growth of China, even with a slowing Chinese economy and higher inflation, as providing a reliable market for Australian commodities exports. ABARE was growing more confident that agricultural commodities would form a greater share of Australian exports to China as global food price rises affected availability in the PRC, Hogan said.

Views about Foreign Direct Investment

14. (SBU) Howard mentioned an independent study, commissioned by Rio Tinto, that analyzed Australians' attitudes towards foreign direct investment in Australia. Howard reported that respondents aged 45 and older were suspicious of Chinese investment in Australia and, while they believed that it was "OK for China to buy from Australia," wanted to know "why China felt it needed to own firms within Australia." They had a relatively sophisticated view of the need for foreign investment, but feared the impact of broader foreign ownership on jobs and pension systems like the Superannuation Fund. Somewhat unexpectedly, Howard said, respondents aged 20-45 were indifferent or apathetic towards foreign direct investment. The younger respondents showed a "discouraging" level of ignorance on the economy as a whole, Howard said. The lunch guests remarked that Australians still appeared to welcome investment from the "Anglosphere" (Canada, the U.K. and U.S.) but were more suspicious of investment by newly developing economies like China.

CANBERRA 00000792 002 OF 002

15. (SBU) Comment: All of our interlocutors noted that Australians, although concerned that Chinese investors might not operate in a transparent, market-driven fashion, had been through a similar experience with Japanese and Korean investment. General opinion was that Australia is well-placed to handle these issues, and that they will not develop into a source of significant tension with Beijing. End comment.

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